

(c)(3)(i) of this section) if and only if such expense is incurred as a result of, or incident to, an activity in which such gross income is derived or in connection with property from which such gross income is derived. For example, general and administrative expenses and compensation paid to officers attributable to the performance of services that do not directly benefit or are not incurred by reason of a particular activity or particular property are not clearly and directly allocable to portfolio income (within the meaning of paragraph (c)(3)(i) of this section).

(5) *Treatment of loss from disposition—*
(i) *In general.* Except as otherwise provided in the regulations under section 469—

(A) Any loss recognized in any year upon the sale, exchange, or other disposition (a “disposition”) of an interest in property used in an activity at the time of the disposition or of an interest in an activity held through a partnership or S corporation and any deduction allowed on account of the abandonment or worthlessness of such an interest is treated as a deduction from such activity; and

(B) Any such deduction is a passive activity deduction if and only if the activity is a passive activity of the taxpayer for the taxable year of the disposition (or other event giving rise to the deduction).

(ii) *Disposition of property used in more than one activity in 12-month period preceding disposition.* In the case of a disposition of an interest in property that is used in more than one activity during the 12-month period ending on the date of the disposition, the amount realized from the disposition and the adjusted basis of such interest must be allocated among such activities in the manner described in paragraph (c)(2)(ii) of this section.

(iii) *Other applicable rules—*

(A) *Applicability of rules in paragraph (c)(2).* [Reserved] See § 1.469-2(d)(5)(iii)(A) for rules relating to this paragraph.

(B) *Dispositions of partnership interests and S corporation stock.* A partnership interest or S corporation stock is not property used in an activity for purposes of this paragraph (d)(5). See paragraph (e)(3) of this section for rules

treating the loss recognized upon the disposition of a partnership interest or S corporation stock as loss from the disposition of interests in the activities in which the partnership or S corporation has an interest.

(6) *Coordination with other limitations on deductions that apply before section 469—*

(i) *In general.* An item of deduction from a passive activity that is disallowed for a taxable year under section 704(d), 1366(d), or 465 is not a passive activity deduction for the taxable year. Paragraphs (d)(6)(ii) and (iii) of this section provide rules for determining the extent to which items of deduction from a passive activity are disallowed for a taxable year under sections 704(d), 1366(d), and 465.

(ii) *Proration of deductions disallowed under basis limitations—*(A) *Deductions disallowed under section 704(d).* If any amount of a partner’s distributive share of a partnership’s loss for the taxable year is disallowed under section 704(d), a ratable portion of the partner’s distributive share of each item of deduction or loss of the partnership is disallowed for the taxable year. For purposes of the preceding sentence, the ratable portion of an item of deduction or loss is the amount of such item multiplied by the fraction obtained by dividing—

(1) The amount of the partner’s distributive share of partnership loss that is disallowed for the taxable year; by

(2) The sum of the partner’s distributive shares of all items of deduction and loss of the partnership for the taxable year.

(B) *Deductions disallowed under section 1366(d).* If any amount of an S corporation shareholder’s pro rata share of an S corporation’s loss for the taxable year is disallowed under section 1366(d), a ratable portion of the taxpayer’s pro rata share of each item of deduction or loss of the S corporation is disallowed for the taxable year. For purposes of the preceding sentence, the ratable portion of an item of deduction or loss is the amount of such item multiplied by the fraction obtained by dividing—

(1) The amount of the shareholder’s pro rata share of S corporation loss that is disallowed for the taxable year; by

(2) The sum of the shareholder's pro rata shares of all items of deduction and loss of the corporation for the taxable year.

(iii) *Proration of deductions disallowed under at-risk limitation.* If any amount of the taxpayer's loss from an activity (within the meaning of section 465(c)) is disallowed under section 465 for the taxable year, a ratable portion of each item of deduction or loss from the activity is disallowed for the taxable year. For purposes of the preceding sentence, the ratable portion of an item of deduction or loss is the amount of such item multiplied by the fraction obtained by dividing—

(1) The amount of the loss from the activity that is disallowed for the taxable year; by

(2) The sum of all deductions from the activity for the taxable year.

(iv) *Coordination of basis and at-risk limitations.* The portion of any item of deduction or loss that is disallowed for the taxable year under section 704(d) or 1366(d) is not taken into account for the taxable year in determining the loss from an activity (within the meaning of section 465(c)) for purposes of applying section 465.

(v) *Separately identified items of deduction and loss.* In identifying the items of deduction and loss from an activity that are not disallowed under sections 704(d), 1366(d), and 465 (and that therefore may be treated as passive activity deductions), the taxpayer need not account separately for any item of deduction or loss unless such item may, if separately taken into account, result in an income tax liability different from that which would result were such item of deduction or loss taken into account separately. For related rules applicable to partnerships and S corporations, see § 1.702-1(a)(8)(ii) and section 1366(a)(1)(A), respectively. Items of deduction or loss that must be accounted for separately include (but are not limited to) items of deduction or loss that—

(A) Are attributable to separate activities (within the meaning of the rules to be contained in § 1.469-4T);

(B) Arise in a rental real estate activity (within the meaning of section 469(i) and the rules to be contained in § 1.469-9T) in taxable years in which the

taxpayer activity participates (within the meaning of section 469(i) and the rules to be contained in § 1.469-9T) in such activity;

(C) Arise in a rental real estate activity (within the meaning of section 469(i) and the rules to be contained in § 1.469-9T) in taxable years in which the taxpayer does not actively participate (within the meaning of section 469(i) and the rules to be contained in § 1.469-9T) in such activity;

(D) Arose in a taxable year beginning before 1987 and were not allowed for such taxable year under section 704(d), 1366(d), or 465(a)(2);

(E) [Reserved] See § 1.469-2(d)(6)(v)(E) for rules relating to this paragraph.

(F) Are attributable to pre-enactment interests in activities (within the meaning of § 1.469-11T(c)).

(7) *Deductions from section 481 adjustment—(i) In general.* If a change in accounting method results in a negative section 481 adjustment with respect to an activity, a ratable portion (within the meaning of paragraph (d)(7)(iii) of this section) of the amount taken into account for a taxable year as a net negative section 481 adjustment by reason of such change shall be treated as a deduction from the activity for such taxable year, and such deduction shall be treated as a passive activity deduction if and only if such activity is a passive activity for the year of the change (within the meaning of section 481(a)). See the rules to be contained in § 1.469-1T(k) for the treatment of passive activity deductions from an activity in taxable years in which the activity is a former passive activity.

(ii) *Negative section 481 adjustments.* For purposes of applying this paragraph (d)(7)—

(A) The term “net negative section 481 adjustment” means the decrease (if any) in taxable income taken into account under section 481(a) to prevent amounts from being duplicated or omitted by reason of a change in accounting method; and

(B) The term “negative section 481 adjustment with respect to an activity” means the decrease (if any) in taxable income that would be taken into account under section 481(a) to prevent only the duplication or omission of